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# THE NATIONAL DEBT

Facts about public spending . . . background information on a big U. S. problem.

The national debt worries a great many people. Some think mounting Federal debts and budget deficits in recent years are forerunners of a crack-up of the government's credit: inflation, chaos. Others say a Federal debt several times the size of the present one would not be dangerous.

Credit is a matter of confidence. If for any reason people generally adopted the attitude that the financial position of the government was unsound, it probably would be unsound. The situation would be the same as a run on a bank, though on a larger scale. The government would be unable to sell its bonds on the open market, the dollar would depreciate, government credit would collapse. Because the financial strength of the government is so much a matter of public attitude, it is important that the public have facts on which to base attitudes.

The following facts are presented with the intention of contributing to sober consideration of the public debt question. The facts are allowed to speak for themselves except where interpretation and explanation are needed for clarity.

The pitfall most people fall into in duscussing public credit is in taking over the same terms and principles as are used in private credit. They forget that: (1) The profit motive of private business is absent. (2) Whereas a private individual should not pay out more than he takes in for any long period, this rule obviously cannot apply to the public as a whole. Excluding unpaid foreign loans, the nation <u>cannot</u> pay out more than its income. Public borrowing is largely a transfer from one group of citizens to another. David Ricardo, an early English economist, said, "A national debt is like a debt of the left hand to the right hand." The nation as a whole is, of course, taxing itself to pay interest to itself. Repudiation of the debt would cause no real loss to the nation; it would simply result in a shift of funds from bondholders to taxpayers. To a large extent these are the same people. (3) A private individual must adjust his debts to his income but a government can adjust its income to its debt within "reasonable" limits.

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The total Federal debt is now more than 39 billion dollars. From the war-time peak of 25 billion dollars, the debt was reduced to less than 17 billion dollars at the beginning of the depression. Since then, it has more than doubled. But these total Federal debt figures, as reported by the Treasury Department, do not give an accurate picture of the actual debt. Much of this debt represents a proprietary interest of the government in such organizations as the RFC, FCA, and others. Some of it represents cash held by the government. When these items are subtracted, the total debt drops to around 31 billion dollars. This "net balance of debt" has not increased as much during the depression as the total debt. In 1930, the low point, it was 15.5 billion dollars.

| Net Balance of Federal Debt* | |
|---|---|
| 1929 | 16.4 |
| 1930 | 15.5 |
| 1931 | 15.8 |
| 1932 | 17.3 |
| 1933 | 19.0 |
| 1934 | 20.2 |
| 1935 | 22.8 |
| 1936 | 27.4 |
| 1937 | 30.5 |

*From Debts and Recovery, by Albert G. Hart and the Committee on Debt Adjustment of the Twentieth Century Fund.

* * *

Two periods of emergency have created our Federal debt. The World War caused huge deficits in 1918 and 1919, and we wound up with a total debt of 25 billion dollars. The depression which began in 1929 caused the government to spend greatly in excess of tax receipts. The President's budget recently submitted to Congress called for another budget deficit in the fiscal year ending June, 1940. This will make 10 consecutive years of deficits. In these 10 years deficits will have mounted to 27 billion dollars.

For these 27 billions, however, the nation has got nearly 16 billion dollars' worth of "real values" including buildings, roads, dams, improved forests, and loans and investments which are largely recoverable. The other 10 billion or more has gone into direct relief, payments to farmers under the AAA and other non-recoverable expenditures. Whether the nation has got its money's worth out of this government spending will always be an argument. Some say a revolution, a social upheaval, was imminent during the depths of the depression--that government spending saved the day. Others say the money has been wasted -- especially that which is non-recoverable.

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How does our public debt compare with that in other countries? If our national government debt per capita is compared with national government debts of other great powers, it looks comfortingly small. But the national debts of most of these other countries are their total public debts. We have large local and state government debts in addition. So to get a fair comparison, our total public debt must be sized up in relation to public debts abroad. Our debt still looks small. Take the British situation for example. The public debt in Great Britain is almost double ours per capita. However, part of Great Britain's debt has been incurred as a result of its business ventures, such as the telephone and telegraph services. To make an absolutely fair comparison, we should have to add the bonded indebtedness of similar private businesses to our public debt. Finances in the dictator countries are not open for public scrutiny, but it appears that these nations are avoiding going deeper into debt by extremely heavy taxes and forced loans.

Taken in relation to income-producing and taxpaying power, our public debt is puny compared with those of most other world powers. Our government has not entered so completely into the economic life of the country as have other national governments. These estimates (from Consumption in Our Society, by Elizabeth Hoyt, Iowa State College) of the percentages governmental expenditures are of national incomes show only Canada with a smaller ratio than the U. S.:

| | | | |
|---|---|---|---|
| Canada | 13 | Great Britain | 29 |
| U. S. | 16 | Italy | 30 |
| Japan. | 24 | Germany | 30 |
| France | 25 | | |

* * *

Who holds the public debt is an important aspect of governmental finance. To the extent that holders of government bonds are taxpayers of equal size, the Federal debt is meaningless. Taxpayers are simply paying themselves interest. But this is true only to a small extent. Credit institutions, mainly banks and insurance companies, are the biggest holders of the Federal debt. Obviously, financial institutions receive far more in interest from government bonds than they pay the government in taxes. A breakdown of government credit and default of its bonds would wreck many banks and insurance companies. Virtually all the increase in the national debt in the last few years has been taken by credit institutions: (From Debts and Recovery.)

| Total Public Debt (Billion Dollars) | | Held by Credit Institutions | Others |
|---|---|---|---|
| 1930. | 16.7 | 5.9 | 10.8 |
| 1935. | 31.3 | 19.3 | 12.0 |
| 1937. | 38.4 | 23.5 | 14.9 |

* * *

The Federal debt looks burdensome in its 11-digit totals, less burdensome after recoverables are subtracted, still less burdensome in terms of carrying charges. Annual interest charges have not increased anything like the total debt. The government has financed an increasing proportion of its loans by short-time notes and bills which currently take a low interest rate. The general level of interest rates has dropped substantially in recent years. Compare these interest charges on the Federal debt with the total interest-bearing debt: (From Annual Report of the Secretary of the Treasury for 1937, and the Federal Reserve Bulletin.)

| | Total Interest Bearing Debt | | Annual Interest Charges | |
|---|---|---|---|---|
| | Millions | Percent | Millions | Percent |
| 1932. . . . | $19,161 | 100 | $599 | 100 |
| 1934. . . . | 26,480 | 138 | 757 | 126 |
| 1936. . . . | 32,989 | 172 | 749 | 125 |
| 1938. . . . | 36,576 | 191 | 926 | 155 |

* * *

Much of the increase in the national debt in recent years has not been an increase in total public debt but merely a shift from state and local governments to the Federal Government. State and local government debts have increased only slightly above the 1929 level during the last 9 years. National government spending has taken up the slack in local relief caused by depleted local government treasuries.

When private investment slumped, the Federal treasury opened up its coffers for loans and grants on many construction projects, poured millions into tottering industries such as the railroads and in general tried to stem the gap in private investment. The following tabulation shows how total capital investment slumped during the depression and how public investment increased. These figures include all public investment, but the increase in recent years is almost entirely Federal.

Capital Formation*
(Billion Dollars)

| | Total | Public |
|---|---|---|
| 1920 . . . . . | 22.1 | 1.7 |
| 1922 . . . . . | 13.3 | 2.4 |
| 1924 . . . . . | 15.2 | 2.5 |
| 1926 . . . . . | 19.0 | 2.6 |
| 1928 . . . . . | 17.8 | 2.7 |
| 1930 . . . . . | 13.7 | 3.3 |
| 1931 . . . . . | 8.5 | 2.5 |
| 1932 . . . . . | 3.1 | 2.0 |
| 1933 . . . . . | 4.3 | 1.7 |
| 1934 . . . . . | 6.1 | 3.8 |
| 1935 . . . . . | 9.0 | 4.9 |

*From National Income and Capital Formation by Simon Kuznets, National Bureau of Economic Research.

Thus, to a larger extent than you may have realized, the increased Federal spending of recent years has been replacement spending.

It has replaced state and local governments and private individuals in relief of the poor and unemployed. It has replaced private capital in many lines of investment.

Your attitude toward the national debt will depend on whether you believe these expenditures were and are worth while.